

CHAPTER 4 – FINANCIAL MANAGEMENT

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CHAPTER 4

FINANCIAL MANAGEMENT

I. OVERVIEW

This chapter provides guidance on the federal and state requirements that govern the financial management of all CDBG funds, so that each local government grantee can maintain an adequate financial system. The financial system maintained must be flexible enough to accommodate applicable laws and regulations and conform to generally accepted accounting principles as well.

II. APPLICABLE FEDERAL AND STATE REQUIREMENTS

A. FEDERAL REQUIREMENTS

The key federal requirements that the grantee must comply with are embodied in the following Office of Management and Budget (OMB) circulars and Federal Housing and Urban Development (HUD) regulations.

1. OMB Circular A-87, Cost Principles for State and Local Governments

This circular establishes the principles for classifying administration costs as direct or indirect and for determining which costs are allowable and unallowable.

2. HUD Administrative Requirements for Grants and Cooperative Agreements to State, Local and Federally Recognized Indian Tribal Governments, 24 CFR, Part 85

These HUD administrative requirements are the basis for a number of financial management requirements on grantees. They are divided into four major subparts and include:

- Subpart A - General
- Subpart B - Pre-award Requirements
- Subpart C - Post-award Requirements:
Financial Administration
 - Changes, Property and Sub-awards
 - Reports, Records, Retention and Enforcement
 - Subpart D - After-the-Grant Requirements

3. HUD (Part II) CDBG State Final Rule, 24 CFR, Part 570

This rule includes HUD's regulations governing the state administration of CDBG funds.

4. HUD (Part III) CDBG Final Rule Regulations, 24 CFR, Part 570, Subpart C - Eligible and Ineligible Activities

These HUD regulations deal specifically with eligibility issues and are, therefore, the controlling regulations in this regard. Subpart C includes the following sections:

- 570.201 Basic eligible activities
- 570.202 Eligible rehabilitation and preservation activities
- 570.203 Special economic development activities
- 570.204 Special activities by certain subrecipients
- 570.205 Eligible planning, urban environmental design and policy-planning-management-capacity building activities
- 570.206 Program administration costs
- 570.207 Ineligible activities

B. STATE REQUIREMENTS

1. Budgetary, Accounting and Reporting Systems (BARS) for Cities, Towns and Counties

The BARS system fulfills all HUD project accounting and reporting requirements (Section 2-7-504).

2. Budgetary Authority

Under Montana law, local governments are required to appropriate, by resolution, all CDBG funds received, regardless of the time the funds are received. The resolution should state the source of the funds, the program in which they will be expended and the effective date of the appropriation (Section 7-6-4006).

3. Surety Bonds

Montana law requires surety bonds for local government officers and employees who are involved in the administration of public funds. The amount of a bond should be based on the amount of money handled and the opportunity for misuse of funds (Sections 2-9-701, 2-9-702 and 2-9-802).

III. PROGRAM REQUIREMENTS

A. PROJECT BUDGET

The budget for the CDBG project is a part of the project Management Plan. Once the Management Plan is approved and the contract signed, specific requirements are placed on the grantee.

1. The grantee, in accordance with Section 7-6-4006, must appropriate, by resolution, the CDBG money received from the MDOC. The resolution must state the source of the money, the program in which money will be expended, and the effective date of the resolution. (See **Exhibit 4-A**)
2. The grantee must expend the grant money in accordance with the provisions of the CDBG project budget. However, the budget may be amended so long as it is not increased or does not violate the conditions under which the grant was awarded. If the amount of the amendment will not exceed \$5,000, the grantee need not request MDOC approval. If the amount will exceed \$5,000, the grantee must request written approval from MDOC.

The preparation, content and approval of the project budget is dealt with in Chapter I, Project Start-Up. Please consult Chapter 1 for related information.

B. PROJECT ADMINISTRATION COSTS

(Please see **Exhibit 4-B** for a detailed description of allowable and unallowable administration costs for CDBG projects.)

C. LOCAL DEPOSITORY ACCOUNT

The grantee is required to establish and maintain a depository account in a local financial institution. The account will be used exclusively for the receipt and disbursement of CDBG funds. There are, however, certain conditions the grantee must meet in the management of the account, including:

1. The grantee must follow the appropriate HUD accounting and financial management procedures required by 24 CFR 85.20.
2. The account must be non-interest bearing. If, however, any interest is earned, it must be returned to MDOC.
3. The time elapse between grantee drawdown and disbursement must be minimized.
 - a. Treasury Circular 1075 requires that state disbursements to a recipient organization must be limited to the minimum amounts needed and must be timed to be in accord with actual, immediate cost requirements of the recipient organization in carrying out the purpose of the approved program or project. The timing and amount of cash advances must be as close as administratively feasible to the actual disbursements by the recipient organization for direct program cost and the proportionate share of any allowable indirect costs.
 - b. HUD has interpreted this provision to mean that no more than \$5,000 may be retained in a grantee's federal depository account for a period longer than three business days.

D. PROJECT DRAWDOWNS

All projects are subject to State and Federal environmental review requirements. Requests for drawdowns must not be made until a Request for Release of Funds has been submitted and approved by MDOC. See Chapter 2, Environmental Review.

If a grantee has generated and retained any “program income” from a past CDBG project (income directly generated from the use of CDBG funds used in a previous CDBG project, see IV. Program Income and Revolving Loans, this chapter), all such program income must be expended before drawing down funds from a current grant award.

To establish the mechanisms for requesting CDBG funds and for receiving them, the grantee must complete the following forms:

1. Signature Certification Form (see **Exhibit 1-D**);
2. Designation of Depository Card (see **Exhibit 1-E**);
3. Designation of Depository for Direct Deposit, if opted for (see **Exhibit 1-E**).

Grantee drawdowns include preparation and submission of:

- The Request For Funds (**Exhibit 4-C**);
- Uniform Status of Funds Spreadsheet (**Exhibit 4-D**);
- The Uniform Invoice Tracking Spreadsheet (**Exhibit 4-E**);

(Completion instructions are included for these preprinted reports. **Drawdown and tracking spreadsheet forms are available on diskette at your request.** The CDBG recipient is required to use the invoice tracking spreadsheet to record all invoices, which will make the spreadsheet reconcilable to the status of funds spreadsheet and other accounting records.

- **Copies of invoices, purchase orders, lease agreements, acquisition agreements, etc.** All expenditures that have been paid in part or totally from CDBG funds, regardless of the amount, must be documented with copies of eligible costs incurred, and itemized in the Project Progress Report;
- Copies of timesheets or other summary payroll information for work performed by city or county employees. Summary information must include at a minimum the name, title, time period, activities performed, and total amount.
- If the CDBG liaison has any questions concerning the appropriateness or amount of an expenditure, copies of more detailed supporting documentation may be required.
- During periods of construction, draws must be accompanied by Exhibit 6-K and 6-P.

NOTE: Contractors providing professional services (i.e. engineering, architectural, project administration) should submit itemized invoices describing services furnished, total hours worked to accomplish each item, amount being billed for each item, a description of any other eligible reimbursable expenses incurred during the billing period, and total amount being billed. In addition, a narrative description in sufficient detail must be submitted to justify the amount claimed on invoice (see Chapter 3, M. Contract Pricing and Method of Compensation.)

Each drawdown request must also be accompanied by a Progress Report. The Progress Report (**Exhibit 4-F**) should provide the CDBG Program Specialist with information on the expected use of the funds requested, status of the project, completed milestones and project progress as it relates to the current implementation schedule. If key dates identified in the current implementation schedule should change, a revised implementation schedule would need to be forwarded to CDBG.

The Request For Payment And Status of Funds Report, Status of Funds and Invoice Tracking Spreadsheets, necessary documentation, and accompanying Progress Report should be mailed to the CDBG Program Specialist, Department of Commerce, Community Development Division, 301 S. Park, P.O. Box 200523, Helena, MT 59620 or faxed to MDOC at 841-2771. If the draw is faxed, original copies should be mailed as soon as possible.

► Minimum amounts for requests for funding: Processing a drawdown request for funds involves staff from several state agencies. In order to reduce the expense for processing requests for funds and to provide the most efficient service to grant recipients, we ask that grant recipients avoid submitting requests for funds that total less than \$1,200, to the extent possible.

Upon receipt, the Request For Payment And Status of Funds Report and Progress Report will be reviewed by CDBG staff.

1. The CDBG staff review the Request for Payment and Progress Report and check:
 - a. The contract number, addresses and bank account number for correctness;
 - b. The reasonableness of the amount requested. Expenditures must be appropriate based upon the description offered for both administration and project activity costs. The amount requested must be consistent with the approved contract budget and the project progress report;
 - c. The eligibility of all costs and their consistency with the contract scope of services;
 - d. The financial numbers for correctness;

- e. The expended to date balances for consistency with the preceding request for payment;
 - f. The percentage of the administration and activity budgets expended, the total amount drawn to date against the amount budgeted and the amount of CDBG funds on hand; and
 - g. The correctness of signatures against the authorized signature form.
- 2. If the information is satisfactory, the CDBG staff signs the Request for Payment and forwards it to the MDOC Management Services Division. The Management Services staff collects the Payment Requests and usually prepares claims for payments twice per week. If the claims process correctly, warrants are prepared and mailed the following business day.
 - 3. If the information is unsatisfactory, the grantee will be notified as to why.

Once the request for payment is approved, the grantee has the option of getting the funds by return mail or direct deposit. The drawdown request should stipulate the preferred option. The turn-around time for receipt of funds by the CDBG recipient is expected to be 7 to 10 business days. Overall, the grantee should expect at least 30 days from the date the contractor submits an invoice to the grantee until receipt of funds from the CDBG program. To expedite routine drawdowns, the grantee should consider using a "master form" to prepare the Request For Payment And Status of Funds Report. The "master" is headed up with only that information that is fixed or must appear on every drawdown. Then, it's just a matter of making a copy of the "master" each time and entering the information that is relative to the current drawdown. Unchanged information is not repeated for each drawdown. A new "master" would only have to be prepared in the case of budget amendments or changes in line item amounts.

E. QUARTERLY REPORTING REQUIREMENTS

The CDBG recipient is required to submit a Project Progress Report each calendar year quarter unless the CDBG recipient has submitted a request for funds to CDBG at some point during the quarter. The Project Progress Report is required within fifteen (15) days following the close of each quarter. When the CDBG recipient is submitting a Project Progress Report to satisfy the quarterly report requirement, the CDBG recipient only needs to include an update to the project status section of the Project Progress Report.

F. TWO PERCENT RETAINAGE

The Department will retain two percent (2%) of the total authorized grant amount until:

- **the project has been completed (a Certificate of Substantial Completion has been**

issued), and

- **a conditional closeout report has been submitted by the CDBG recipient and approved by the Department.**

This amount will be withheld at the end of the project not from each request for funds. Once a conditional closeout has been submitted and approved by the Department, the two percent (2%) retainage will be released to the CDBG recipient. (For more information on the release of the retained funds at closeout, refer to Chapter 13 - Project Closeout.)

G. INTERIM FINANCING

The environmental review process or unforeseen circumstances could, occasionally, delay the receipt of CDBG funds. In either event, the grantee may need or want to secure other interim financing. **Please consult MDOC for approval prior to incurring any financing costs.**

The local government grantee has the following interim financing options:

1. Under Attorney General opinion number 14, volume 38, it may borrow money directly from a financial institution;
2. Under Section 7-7-109, it may sell notes in anticipation of receiving a grant or loan from federal or state sources;
3. Counties and municipalities may make interfund loans in lieu of registering warrants under Generally Accepted Accounting Principles.
4. Under Sections 7-13-2221 (county water and sewer districts) and 7-13-236 (solid waste districts), they may borrow money, in addition to the issuance of bonds, for construction purposes and the purchase of equipment.

H. PROPERTY MANAGEMENT AND DISPOSITION

(Please refer to **Exhibit 4-G** – Federal Regulations for Real Property)

I. RETENTION - DOCUMENTS/RECORDS/REPORTS

Under HUD regulations, the documents, records and reports described below must be retained for three years after project closeout. However, in the event of litigation, claim, negotiation audit or other action, such documents, records and reports must be retained until completion of the action or regular time period, whichever is later.

1. Documents:

- Receipt
- Purchase order
- Expenditure review
- Invoice/statement
- Claim
- Check
- Warrant

2. Records:

- Accounting
- Budgetary
- Payroll
- Time
- Bank statement

3. Reports:

- Financial statement/monthly and annual
- Budgetary/monthly and annual
- Payroll
- Request For Payment And Status Report
- Progress Report
- Payment Certification

4. Other:

- Budgetary Resolution
- Signature Certification
- Designation of Depository

These documents, records and reports are subject to applicable federal, state and local laws relating to public access, privacy and confidentiality.

IV. PROGRAM INCOME AND REVOLVING LOANS

Because of HUD's reemphasis on its policies dealing with program income and the related amendments to the Housing and Community Development Act, MDOC established guidelines for local government grantees that retain and use program income in the *CDBG Program Income and Revolving Loan Fund Manual* (Montana Department of Commerce, January, 1996). These guidelines also address the other side of the program income equation -- the area of revolving loans.

The guidelines focus on state oversight and local government management of and accountability for program income and revolving loans. (Please see **Exhibit 4-H**, Program Income.)

V. GENERAL ACCOUNTING REQUIREMENTS

A. STANDARDS FOR ACCOUNTING SYSTEMS

The grantee (under HUD 24 CFR, 85.20) is required to maintain accounting records that adequately identify the source and application of funds provided for CDBG assisted activities. The records must also contain information pertaining to assets, liabilities, expenditures and income.

Accountability for CDBG funds, as embodied in the above HUD regulation, requires adequate assurance that these funds are used solely for authorized purposes. This requirement is best met through fund accounting.

B. FUND ACCOUNTING

Fund accounting is a control device to segregate resources and ensure that the segregated resources are only used for their intended purposes.

Grantee accounting systems should be organized and operated on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

Governmental accounting standards require that local governments use a fund accounting system. The Montana BARS System for Counties, Cities and Towns is a fund accounting system that meets all fund accounting requirements. (see Exhibits K, L and M)

C. FUND TYPE AND ACCOUNT GROUP TO BE UTILIZED

There are a number of funds and account groups that are required to be utilized in a fund accounting system, each depending on the financial situation. However, the CDBG grantee need only be concerned with the following fund types and account group:

1. Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than capital asset grants) that are legally restricted to expenditures for specified CDBG purposes.
2. Capital Projects Funds are used to account for non-enterprise fund capital asset grants and for pass-through capital asset grants. (Pass-through capital asset grants are discussed below.)

In Statement No. 24, "Accounting and Financial Reporting for Certain Grants and Other Financial Assistance", the Governmental Accounting Standards Board (GASB) discusses and prescribes procedure for treatment of pass-through grants:

" . . . Governmental entities often receive grants and other financial assistance to transfer to or spend on behalf of a **secondary recipient**. These amounts are referred to as pass-through grants. All cash pass-through grants received by a government entity, (referred to as a **recipient government**) should be reported in its financial statements. As a general rule, cash pass-through grants should be recognized as revenues and expenditures or expenses in a governmental, proprietary or trust fund. In those infrequent cases in which a recipient government serves only as a cash conduit, the grant should be reported in an agency fund. A recipient government serves only as a cash conduit if it merely transmits grantor-supplied moneys without having administrative or direct financial involvement in the program. A recipient government has administrative involvement if, for example, it (a) monitors secondary recipients for compliance with program-specific requirements, (b) determines eligible secondary recipients or projects, even if using grantor-established criteria, or (c) has the ability to exercise discretion in how the funds are allocated. A recipient government has direct financial involvement if, for example, it finances some direct program costs because of a grantor-imposed matching requirement or is liable for disallowed costs . . . "

3. The General Fixed Asset Account Group is used to account for non-enterprise capital asset grants where ownership vests with the grantee.
4. Enterprise Funds are used to account for capital asset grants utilized in water, sewer or solid waste systems.

The above funds and account group will each be structured with a set of self-balancing accounts, in which to record all appropriate CDBG financial transactions.

D. BASIS OF ACCOUNTING

The basis of accounting is a term used to refer to when revenues and expenditures/expenses, and the related assets and liabilities, are recognized in the accounts and reported in the financial statements.

There are three fundamental accounting bases used to account for transactions, the cash basis, the accrual basis and the modified accrual basis. The basis for Special Revenue Funds and Capital Projects Funds is the modified accrual basis. For enterprise funds, it is the accrual basis.

Under the modified accrual basis, revenues are recognized when they become susceptible to accrual, that is, when they become both "measurable" and "available" to finance expenditures of the current period. Available means collectible in the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recognized when the fund liability is incurred.

Under the accrual basis, revenues are recognized when they are earned and become measurable. Expenses recognized in the period incurred, if measurable.

E. FUND AND ACCOUNT STRUCTURE

The chart of accounts is the framework around which the accounting system is built. A chart of accounts is merely a numerical coding system that permits identification of individual accounts. It also simplifies the referencing of entries on documents and records and helps reflect account relationships.

Balance sheet accounts are those accounts that remain open after the books have been closed at year-end, the balances of which are carried forward into the succeeding year. When properly classified, these accounts form the basis for the balance sheet. Simply put, the balance sheet purports to exhibit what a fund owns in the form of assets and what a fund owes in the form of liabilities, the net result of which (assets minus liabilities) is equity.

Revenues should be classified by source. The primary functions of revenue accounts are to provide a means for verifying the receipt of revenues and to furnish information for preparing financial reports. Revenue accounts are closed out at year-end.

Expenditures should be classified by function, activity and object. The function classification provides information on the overall purposes or objectives of expenditures. The activity classification provides information according to the specific types of work performed by the organizational unit. The object classification relates to the article purchased or service obtained. The primary functions of expenditure accounts are to provide proper control (**Exhibit 4-I**) and furnish information for preparing financial reports. Expenditure accounts are closed out at year-end.

The coding system that follows is consistent with CDBG needs and is made up of fund identifiers and balance sheet, revenue and expenditure accounts.

The fund code identifiers assigned to the required CDBG funds are:

<u>Special Revenue Funds</u>	<u>Fund/Range</u>
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<i>I. Housing and Rehabilitation</i>	<i>2940</i>
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a. Balance sheet accounts:

<u>Account Number</u>	<u>Account Name</u>
101000	Cash
102160	Escrow Cash
102165	Program Income Cash/92
102166	Program Income Cash/93
125000	Loans Receivable
172000	Revenue Control

201100	Warrants Payable
202100	Accounts Payable
204000	Contracts/Loans Payable (short term)
223800	Deferred Revenue
235100	Contracts/Loans Payable (long term)
242000	Expenditure Control
271000	Fund Balance

b. Revenue accounts:

<u>Account Number</u>	<u>Account Name</u>
331010	CDBG Grants
362000	Miscellaneous
373010	Interest
373020	Principal

c. Expenditure accounts:

470200	Housing Rehabilitation
470210	Administration
	100 Personal Services
	200 Supplies
	310 Postage
	320 Printing/Duplicating
	330 Advertising/Publications
	340 Telephone
	350 Legal
	351 Accounting/Auditing
	352 Consulting
	353 LGS Technical Assistance
	370 Travel/Training
	700 Grants and Loans
	800 Other
470220-75x	Acquisition of Property
470230-75x	Public Works Facilities
470240-75x	Rehabilitation Loans/Grants
470250-75x	Relocation Payments
470260-75x	Planning and Management
470270-75x	Clearing and Demolition
470280-75x	Code Enforcement
470290-75x	Provision of Public Service

The illustrative accounting entries that follow represent those most commonly associated with CDBG funds on a recurring basis. These illustrations are not intended to be all inclusive, but they are intended to exhibit a cross-section of pertinent entries - without undue repetition.

HOUSING REHABILITATION SPECIAL REVENUE FUND

1. *The grantee requested and received a \$100,000 drawdown of CDBG funds.*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>	<u>Sub</u>
2940-101000	Cash	\$100,000		
2940-172000	Revenue Control		\$100,000	
2940-331010	Grants			\$100,000

(To record the receipt of grant funds. Ordinarily, this entry would be recorded as a part of the cash receipt process.)

Related Accounting Procedures

- A receipt document would be issued for the drawdown proceeds and the proceeds promptly deposited to the Local CDBG Depository Account.
- The receipt document would be entered in the Cash Receipts Journal and later posted to accounts in the General Ledger.

2. *The grantee spent \$800 for personal services, \$100 for supplies and \$100 for printing, all chargeable to the administration activity.*

Related Accounting Entries

		<u>Debit</u>	<u>Sub</u>	<u>Credit</u>
2940-242000	Expenditure Control	\$1,000		
2940-470210-100	Personal Services		\$800	
2940-470210-200	Supplies		\$100	
2940-470210-320	Printing/Duplicating		\$100	
2940-101000	Cash			\$1,000

(To record payment of administration expenses. Ordinarily, this entry would be recorded as a part of the cash disbursement process.)

Related Accounting Procedures

- The appropriate warrants or checks would be drawn, signed by the designated persons and delivered or mailed to the respective parties.
- The warrants or checks would be entered in the Cash Disbursement Journal and later posted to accounts in the General Ledger.

3. *The grantee agreed to loan Mr. & Mrs. Doe \$99,000 to refurbish a multiple housing unit. The grantee spent, on behalf of Mr. & Mrs. Doe, \$99,000 on the unit.*

Related Accounting Entries

		<u>Debit</u>	<u>Sub</u>	<u>Credit</u>
2940-242000	Expenditure Control	\$99,000		
2940-470240-75x	Rehabilitation Loans		\$99,000	
2940-101000	Cash			\$99,000

(To record payment for multiple housing unit. Ordinarily, this entry would be recorded as a part of the cash disbursement process.) ***For a more detailed BARS chart of accounts please see Exhibit 4-K.***

2396-125000	Loans Receivable	\$99,000		
2396-223800	Deferred Revenue			\$99,000

(To record the loan receivable. This entry requires the preparation of a general journal voucher.)

Related Accounting Procedures

- The appropriate warrants or checks would be drawn, signed by the designated persons and delivered or mailed to the respective parties.
 - The warrants or checks would be entered in the Cash Disbursement Journal and later posted to accounts in the General Ledger.
 - A general journal voucher (GJV) would be used to book the loan receivable and later the information would be posted to accounts in the General Ledger.
 - Authoritative literature on accounting for housing loans, often referred to as revolving loans, is skimpy at best. The December, 1989 GAAFR Review, published by the Government Finance Officers Association, discusses the pros and cons of several possible treatments - each having some theoretical defect. However, the treatment most favored is to report the loan receivable on the balance sheet at year-end with a corresponding amount of deferred revenue. The above related loan illustration reflects this treatment and is the one that's recommended.
4. *Mr. & Mrs. John Doe made the first payment of principal and interest on their housing loan. The amortized loan is for 20 years at the interest rate of 5 percent per annum. The amount due, according to the amortization schedule, is \$395 for principal and \$475 for interest, a total of \$870.*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>	<u>Sub</u>
2396-102165	Program Income Cash/92	\$870		
2396-172000	Revenue Control		\$870	
2396-373010	Interest			\$475
2396-373020	Principal			\$395

(To record receipt of housing loan payment. Ordinarily, this entry would be recorded as part of the cash receipt process.)

2396-223800	Deferred Revenue	\$395	
2396-125000	Loans Receivable		\$395

(To record the amount of principal paid by the Doe's on their housing loan. This entry requires the preparation of a general journal voucher (GJV).)

Related Accounting Procedures

- A receipt document would be issued for the principal and interest proceeds and the proceeds promptly deposited to the Local CDBG Depository Account.
 - The receipt document would be entered in the Cash Receipts Journal and later posted to accounts in the General Ledger.
 - A general journal voucher (GJV) would be used to record the principal paid by the Doe's on their housing loan and later the information would be posted to accounts in the General Ledger.
 - The loan amortization schedule(s) would serve as the subsidiary loan receivable record.
5. *At year-end, all revenue and expenditure accounts are closed-out to fund balance. Assuming that the preceding transactions represent the entire year's business, the following would be the closing entries.*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>
2940-172000	Revenue Control	\$100,000	
2940-242000	Expenditure Control		\$100,000
2396-172000	Revenue Control	\$870	
2396-272000			\$870

(To record year-end closing.)

Related Accounting Procedures

- A general journal voucher (GJV) would be used for the closing entries and later the information would be posted to accounts in the General Ledger.
-

Special Revenue Funds

Fund/Range

II. Economic Development

2397

2941

a. Balance sheet accounts:

<u>Account Number</u>	<u>Account Name</u>
101000	Cash
102165	Program Income Cash/92
102166	Program Income Cash/93
125000	Loans Receivable
172000	Revenue Control
201100	Warrants Payable
202100	Accounts Payable
204000	Contracts/Loans Payable (short term)
223800	Deferred Revenue
235100	Contracts/Loans Payable (long term)
242000	Expenditure Control
271000	Fund Balance

b. Revenue accounts:

<u>Account Number</u>	<u>Account Name</u>
331010	CDBG Grants
362000	Miscellaneous
373010	Interest
373020	Principal

c. Expenditures accounts:

470300	Economic Development
470310	Administration
	100 Personal Services
	200 Supplies
	310 Postage
	320 Printing/Duplicating
	330 Advertising/Publications
	340 Telephone
	350 Legal

351 Accounting/Auditing
 352 Consulting
 353 LGS Technical Assistance
 370 Travel/Training
 700 Grants and Loans
 800 Other
 470320-75x Economic Development
 Loans
 470330-75x Other

The illustrative accounting entries that follow represent those most commonly associated with CDBG funds on a recurring basis. These illustrations are not intended to be all inclusive, but they are intended to exhibit a cross-section of pertinent entries - without undue repetition.

ECONOMIC DEVELOPMENT SPECIAL REVENUE FUND

1. *The grantee loaned the ABC Company \$50,000.*

Related Accounting Entries

		<u>Debit</u>	<u>Sub</u>	<u>Credit</u>
2941-242000	Expenditure Control	\$50,000		
2941-470320-75x	Economic Develop. Loan		\$50,000	
2941-101000	Cash			\$50,000

(To record loan payment. Ordinarily, this entry would be recorded as a part of the cash disbursement process.)

2397-125000	Loan Receivable	\$50,000		
2397-223800	Deferred Revenue			\$50,000

(To record loan receivable. This entry requires the preparation of a general journal voucher.)

Related Accounting Procedures

- The appropriate warrants or checks would be drawn, signed by the designated persons and delivered or mailed to the respective parties.
- The warrants or checks would be entered in the Cash Disbursement Journal and later posted to accounts in the General Ledger.
- A general journal voucher (GJV) would be used to book the loan receivable and later the information posted to accounts in the General Ledger.

- Authoritative literature on accounting for loans, often referred to as revolving loans, is skimpy at best. The December, 1989 GAAFR Review, published by the Government Finance Officers Association, discusses the pros and cons of several possible treatments, each having some theoretical defect. However, the treatment most favored is to report the loan receivable on the balance sheet at year-end with a corresponding amount of deferred revenue. The above related loan illustration reflects this treatment and is the one that's recommended.
2. *The ABC Company made the first annual payment on their business loan. The amortized loan is for 10 years at the interest rate of 6 percent per annum. The amount due, according to the amortization schedule, is \$5,000 for principal and \$3,000 for interest, a total of \$8,000.*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>	<u>Sub</u>
2397-102165	Program Income Cash/92	\$8,000		
2397-172000	Revenue Control		\$8,000	
2397-373010	Interest			\$3,000
2397-373020	Principal			\$5,000

(To record receipt of business loan payment. Ordinarily, this entry would be recorded as part of the cash receipt process.)

2397-223800	Deferred Revenue	\$5,000		
2397-125000	Loans Receivable		\$5,000	

(To record the amount of principal paid by ABC on their business loan. This entry requires the preparation of a general journal voucher (GJV).

Related Accounting Procedures

- A receipt document would be issued for the principal and interest proceeds and the proceeds promptly deposited to the local CDBG Depository Account.
- The receipt document would be entered in the Cash Receipts Journal and later posted to accounts in the General Ledger.
- A general journal voucher (GJV) would be used to record the principal paid by ABC on their business loan and later the information would be posted to accounts in the General Ledger.
- The loan amortization schedule(s) would serve as the subsidiary loan receivable record.

Special Revenue Funds

Fund/Range

III.	CDBG-Local Source (Loan Repayment-1992 and prior combined)	2392
	CDBG-Local Source-1993 and Later Loan Repayment-Combined	2395
	CDBG-Local Source-1993 and Later Loan Repayment-Housing	2396
	CDBG-Local Source-1993 and Later Loan Repayment-Economic Development	2397

*****These funds will be used on the local level for the granting and repayment of loans from the subrecipients.***

Capital Projects Funds

Fund/Range

IV.	Public Facility Projects: Federal/State Capital Asset Grants (Asset ownership vests with grantee)	4300-4399
	Public Facility State/State Capital Asset Grants (Assets transferred to secondary recipient)	4400-4499

a. Balance sheet accounts:

<u>Account Number</u>	<u>Account Name</u>
101000	Cash
172000	Revenue Control
201100	Warrants Payable
202100	Accounts Payable
242000	Expenditure Control
271000	Fund Balance

b. Revenue accounts:

<u>Account Number</u>	<u>Account Name</u>
331010	CDBG Grants
362000	Miscellaneous

c. Expenditure accounts:

470100	Public Facilities Projects
470110	Administration
	100 Personal Services
	200 Supplies
	310 Postage
	320 Printing/Duplicating
	330 Advertising/Publications
	340 Telephone
	350 Legal
	351 Accounting/Auditing
	352 Consulting

353 LGS Technical Assistance
370 Travel/Training
700 Grants and Loans
800 Other
470120-9xx Construction
470130-9xx Other

The illustrative accounting entries that follow represent those most commonly associated with CDBG funds on a recurring basis. These illustrations are not intended to be all inclusive, but they are intended to exhibit a cross-section of pertinent entries – without undue repetition.

PUBLIC FACILITY CAPITAL PROJECTS FUND

1. *The grantee requested and received \$150,000 drawdown of CDBG funds, to be used in the construction of a \$150,000 community center.*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>	<u>Sub</u>
4300-102100	Construction Cash	\$150,000		
4300-172000	Revenue Control		\$150,000	
4300-331010	Grants			\$150,000

(To record receipt of grant funds. Ordinarily, this entry would be recorded as a part of the cash receipt process.)

Related Accounting Procedures

- A receipt document would be issued for the drawdown proceeds and the proceeds promptly deposited to the Local CDBG Depository Account.
- The receipt document would be entered in the Cash Receipts Journal and later posted to accounts in the General Ledger.

2. *The grantee paid the community center contractor a \$145,000.*

Related Accounting Entries

		<u>Debit</u>	<u>Sub</u>	<u>Credit</u>
4300-242000	Expenditure Control	\$145,000		
4300-470120-9xx	Construction		\$145,000	
4300-102100	Construction Cash			\$145,000

(To record payment of construction costs. Ordinarily, this entry would be recorded as a part of the cash disbursement process.)

Related Accounting Procedures

- The appropriate warrants would be drawn, signed by the designated persons and delivered or mailed to the respective parties.
 - The warrants would be entered in the Cash Disbursement Journal and later posted to accounts in the General Ledger.
3. *At year-end, the revenue and expenditure accounts are closed-out.*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>
4300-172000	Revenue Control	\$150,000	
4300-242000	Expenditure Control		\$145,000
4300-271000	Fund Balance		\$5,000
(To record year-end closing.)			

Related Accounting Procedures

- A general journal voucher (GJV) would be used for the closing entries and later the information would be posted to accounts in the General Ledger.

a.	<u>General Fixed Asset Account Group</u>	<u>Fund/Range</u>
	<i>For Capital Projects Fund Assets</i>	<i>9000</i>
	<i>(Asset ownership vests with grantee)</i>	

Balance sheet accounts:

<u>Account Number</u>	<u>Account Name</u>
181000	Land
182000	Buildings
184000	Improvements other than Buildings
186000	Machinery and Equipment
188000	Construction Work in Progress
280000	Investment in General Fixed Assets

The illustrative accounting entries that follow represent those most commonly associated with CDBG funds on a recurring basis. These illustrations are not intended to be all inclusive, but they are intended to exhibit a cross-section of pertinent entries - without undue repetition.

GENERAL FIXED ASSET ACCOUNT GROUP

1. *The community center was completed during the fiscal year in which it was started. This entry will be made in the general fixed asset account group.*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>
9000-181000	Land	\$25,000	
9000-182000	Buildings	\$125,000	
9000-280000	Investment in Fixed Assets		\$150,000
(To record general fixed assets.) <i>Please see Exhibit 4-K, BARS Chart of Accounts.</i>			

Related Accounting Procedures

- A general journal voucher (GJV) would be used and later the information would be posted to accounts in the General Ledger.

Enterprise Funds

Fund/Range

V. Public Facility Projects Capital Asset Grants:

<i>Water</i>	<i>5210</i>
<i>Sewer</i>	<i>5310</i>
<i>Solid Waste</i>	<i>5410</i>

a. Balance sheet accounts:

<u>Account Number</u>	<u>Account Name</u>
101000	Cash
102110	Construction Cash
172000	Revenue Control
188000	Construction Work in Progress
189xxx	Utility Plant
189xxx	Allowance for Depreciation
201100	Warrants Payable
202100	Accounts Payable
242000	Expenditure Control
2601xx	Contributed Capital
271000	Retained Earnings

b. Revenue accounts:

<u>Account Number</u>	<u>Account Name</u>
331010	CDBG Grants
362000	Miscellaneous

c. Expenditure accounts:

(1) Activity Expenditure Accounts

430500 Water Utilities

- 430510 Administration
- 430520 Facilities
- 430530 Source of Supply and Plumbing
- 430540 Purification and Treatment
- 430550 Transmission and Distribution
- 430570 Customer Accounting and Collection
- 430590 Other Activities

430600 Sewer Utilities

- 430610 Administration
- 430620 Facilities
- 430630 Collection and Transmission
- 430640 Treatment and Disposal
- 430650 Laboratory and Testing
- 430660 Engineering (Undistributed Costs)
- 430670 Customer Accounting and Collection
- 430890 Other Activities

430800 Solid Waste Services

- 430810 Administration
- 430820 Facilities
- 430830 Collection
- 430840 Disposal
- 430870 Customer Accounting and Collection
- 430890 Other Activities

(2) Object of Expenditure Accounts

- 100 Personal Services
- 200 Supplies
- 310 Postage
- 320 Printing/Duplicating

330	Advertising/Publications
340	Telephone
350	Legal
351	Accounting/Auditing
352	Consulting
353	LGS Technical Assistance
370	Travel/Training
700	Grants and Loans
800	Other
900	Capital Outlay

The illustrative accounting entries that follow represent those most commonly associated with CDBG funds on a recurring basis. These illustrations are not intended to be all inclusive, but they are intended to exhibit a cross-section of pertinent entries - without undue repetition.

PUBLIC FACILITY ENTERPRISE FUND

- A. *The grantee requested and received \$100,000 of CDBG funds, to be used in the construction of a water main costing \$100,000 (special interim treatment).*

Related Accounting Entries

		<u>Debit</u>	<u>Credit</u>	<u>Sub</u>
5210-102110	Construction Cash	\$100,000		
5210-172000	Revenue Control		\$100,000	
5210-331010	Grants			\$100,000

(To record receipt of grant funds. Ordinarily, this entry would be recorded as a part of the cash receipt process.)

Related Accounting Procedures

- A receipt document would be issued for the drawdown proceeds and the proceeds promptly deposited to the Local CDBG Depository Account.
 - The receipt document would be entered in the Cash Receipts Journal and later posted to accounts in the General Ledger.
 - At year-end, the respective accounts must be adjusted (reversed) so that all nominal accounts and all permanent accounts are reflected properly in the general accounting records.
2. *The grantee paid the water main contractor \$100,000 (Special interim treatment).*

Related Accounting Entries

		<u>Debit</u>	<u>Sub</u>	<u>Credit</u>
5210-242000	Expenditure Control	\$100,000		
5210-430550-9xx	Transmission/Distribution		\$100,000	
5210-102110	Construction Cash			\$100,000

(To record payment of construction costs. Ordinarily, this entry would be recorded as a part of the cash disbursement process.) ***For a more detailed BARS chart of accounts please see Exhibit 4-K.***

Related Accounting Procedures

- The appropriate warrants would be drawn, signed by the designated person and delivered or mailed to the respective parties.
 - The warrants would be entered in the Cash Disbursement Journal and later posted to accounts in the General Ledger.
 - At year-end, the respective accounts must be adjusted (reversed) so that all nominal accounts and all permanent accounts are reflected properly in the general accounting records.
3. *The water main was placed in service on December 31, 19xx. The estimated service life is 50 years, with zero salvage value. The straight line method of depreciation is used for one year. (\$100,000/50 years = \$2,000 per year)*

Related Accounting Entries

		<u>Debit</u>	<u>Sub</u>	<u>Credit</u>
5210-242000	Expenditure Control	\$2,000		
5210-430550-840	Depr. Expense		\$2,000	
5210-189410	Allow. For Depr			\$2,000

(To record depreciation expense and allowance for depreciation for one year.)

Related Accounting Procedures

- A general journal voucher (GJV) would be required to record the information and later it would be posted to accounts in the General Ledger.
- Under the standards, depreciation recognized on assets acquired through capital grants may be closed to either retained earnings (830) or contributed capital (840). However, the contributed capital option is preferred for capital grants and the one encouraged to be used.

5. Optional Treatment Of Certain Enterprise Fund Transactions

The proceeds from capital grants and loans, etc., may be treated as revenue on an interim basis during the fiscal year. And, similarly, the payments made for capital outlay and the principal portion of debt service, etc., may be treated as an expense on an interim basis during the fiscal year. This departure provides a level of simplicity and a visibility of transactions on interim reports that otherwise would not occur.

At year-end, the respective accounts must be adjusted (reversed) so that all nominal accounts and all permanent accounts are reflected properly in the general accounting records.

F. FIXED ASSET ACCOUNTING

Fixed assets are long-lived tangible assets obtained or controlled as a result of past transactions, events or circumstances. Fixed assets may include buildings, equipment, or improvements other than buildings and land.

They are acquired with cash or cash in conjunction with a trade-in, constructed, and acquired through lease agreement, grant, gift, or donation. Fixed assets acquired should be recorded at historic cost, or if not practically determinable, at estimated historic cost. Donated fixed assets should be recorded at their fair market value when received.

The cost of a fixed asset should include not only its purchase price or construction cost, but also any other reasonable and necessary costs incurred to place the asset in its intended location or use. Such costs could include the following:

- Administration fees/costs
- Legal and title fees
- Appraisal or negotiation fees
- Surveying fees
- Transportation charges
- Insurance premiums during construction
- Demolition costs
- Architect and accounting fees
- Site preparation costs
- Damage payments
- Interest costs during construction

1. Governmental Funds

Generally accepted accounting principles require that fixed assets of a government not reported in a proprietary fund or a trust fund be reported in a General Fixed Assets Account Group (GFAAG). This account group is not a fund; it does not have a balance sheet as such, nor does it report operations. Instead, the GFAAG serves as a list of the government's fixed assets and is designed to ensure accountability. Because the account group does not report operations, all additions and deletions to the GFAAG should be recorded by direct adjustment to the accounts appearing on the entity's combined balance sheet.

The Governmental Accounting Standards Board specifically allows governments the option of not reporting infrastructure fixed assets (i.e., sidewalks, gutters, bridges) in the GFAAG. By definition, infrastructure assets are immovable and of value only to the governmental unit. Therefore, some have argued that there is less need for an accountability listing of such assets because the risk of their being lost or stolen is considerably less than that of other fixed assets. Such an argument, however, fails to take into account the potential losses that can result from poor maintenance or general neglect.

The assets reported in the GFAAG normally are presented by class (land, buildings, improvements other than buildings, equipment). The total amount of these assets is offset by investment in general fixed asset accounts that normally provide details on the source of funding for these assets (other governments, individuals, capital projects, grants). The Investment in General Fixed Assets Account is presented as another credit with government's equity accounts.

Because an account group does not report operations, no charge for depreciation can be reported in the account group. Therefore, assets reported in the GFAAG normally continue to be reported at their original cost until disposal. However, GAAP provides the option of reporting accumulated depreciation on these assets. Because no charge for depreciation can be reported, this account is established by directly reducing the investment in the general fixed asset account and crediting accumulated depreciation for the same amount.

2. Enterprise Funds

Enterprise fixed assets are not recorded in the General Fixed Asset Group of Accounts. Instead, they are accounted for as fund assets of the enterprise itself. The treatment differs because enterprise fixed assets are utilized in revenue producing activities, and the performance measure of an enterprise is the periodic determination of net income. In the net income determination process, GAAP requires a proper matching of all costs associated with the production of revenues. Depreciation of fixed assets used in the production of revenues is a proper element of such costs, therefore, enterprise fixed assets are to be capitalized and depreciated in the fund generating the revenues.

Depreciation is the expiration in the service life of fixed assets, except land, attributable to wear and tear, deterioration, action of the physical elements, inadequacy and obsolescence. Depreciation is defined as a rational and systematic method of distributing the cost of a capital asset over its estimated service life.

Depreciation is an important element in the income determination process of an enterprise. The method used to allocate the cost of a capital asset over its estimated service life should be as equitable as possible to the periods in which services are obtained from the use of the asset. By far, the most common approach used in practice is the straight-line method.

The straight-line method of depreciation simply requires that the cost of the fixed asset (less projected salvage value) be divided by the number of years of estimated service life to arrive at the annual depreciation charge. Estimated service life is the length of time a fixed asset can be expected to perform the function for which it was intended. (Refer to Example C on page 47.)

3. Fixed Asset Policy Guidelines

Inadequate fixed asset records continue to be one of the major causes of deficiencies in most local government's financial statements. Failure to maintain a fixed asset system usually results in a qualification in the independent auditor report (opinion) on the government.

On the other hand, an adequate fixed asset system can result in measurable benefits that provide:

- a. Conformity with generally accepted accounting principles;
- b. Reliable information about fixed assets now owned. Because capital budgets are best developed on a long-term basis, such information is invaluable in projecting future requirements;
- c. Assistance in maintaining accountability for the custody of individual items and in determining who is responsible for their care and maintenance;
- d. Information necessary to perform regular inventories to determine physical condition, theft, or unauthorized transfers;
- e. The ability to identify worn out or obsolete equipment on a concurrent basis. Provision for replacement can be included in a budget before emergency replacement or unwarranted repairs are necessary;

- f. A basis for adequate insurance coverage on insurable fixed assets. Although cost is not the only determinant of insurable value, it could be a necessary consideration;
- g. Property records that furnish information about the investment taxpayers have made for the future benefit to users of government policy;

A number of critical decisions must be made, however, before an adequate fixed asset policy can be established and implemented. Some of those decisions are:

- a. Which asset types should be included? For example, should the infrastructure general fixed assets be included in the system?
- b. Which assets should be accounted for individually and which should be grouped? For example, should the cost of a fire engine include hoses, ladders, and other associated equipment?
- c. What should the capitalization policy be? This sets the requirements for minimum costs to be accounted for and useful lives.
- e. What are the expected useful lives for the different kinds of fixed assets?
- f. What depreciation method is best? Should the government accumulate depreciation on general fixed assets?
- g. When should depreciation begin for assets acquired during the year? For example, depreciation can begin the month the asset is put into service, or a full year's depreciation can be reported for assets received in the first six months and none for those received during the balance of the year. Still, other governments use the half-year convention where fifty percent of the year's depreciation is taken in the year of addition and in the year of disposition.
- h. What information is needed to begin and maintain the system? Determine data base requirements, the coding system and required reports.
- i. Which forms are needed to secure the required information? Their design must ensure complete information and efficient processing.
- j. How will the system be established? A work plan should fix responsibility and establish time estimates. In particular, the initial inventory must be planned thoroughly.
- k. What other policy decision should be established? All policy decisions should be made before beginning work on the fixed asset system. This includes all aspects of the remaining steps -- assigning carrying values and maintaining the system.

A critical step in establishing a fixed asset accounting and reporting system is to establish procedures that will keep the records current. All previous efforts will become outdated and useless unless the information can be updated.

G. BASIC ACCOUNTING RECORDS

The books of account maintained are assumed to be on the double entry system. A double-entry system is defined as a system that requires for every entry made to the debit side of an account(s), an entry for a corresponding amount(s) be made to the credit side of another account(s).

Two types of records are required to account for CDBG funds - the books of original entry and the books of final entry. The books of original entry are those records in which transactions are recorded for the first time, i.e., the Cash Receipts Journal, the Cash Disbursement Journal and the General Journal Voucher. The books of final entry are the summary records in which accounting information is accumulated for financial reporting, i.e., the General Ledger. In an automated environment, however, a single transaction may be recorded simultaneously in the books of original entry and in the books of final entry.

The required books of original and final entry are described below.

- **Cash Receipts Journal**

All cash received is recorded in this book of original entry.

- **Cash Disbursement Journal**

All cash disbursed is recorded in this book of original entry.

- **General Journal Voucher**

All transactions in place of, or supplemental to, the regular journals are recorded in this book of original entry. The voucher is a substitute for maintaining a formal General Journal.

- **General Ledger**

The General Ledger is the book of final entry, where all summarized journal transactions are posted. It contains the accounts needed to present, after closing, the financial representations of the organizational unit.

It is virtually impossible to discuss the books of original entry without discussing their relationship to source documents. Specifically, source documents are documents upon which evidence of an accounting transaction are initially recorded. They may be internally or externally created and are used as the source of entry and support to the various books of original entry. Examples of source documents are general receipts, purchase orders, invoices, claims, payroll time records, contracts, etc.

H. FINANCIAL REPORTS

The financial statements of the grantee must present fairly its financial position and results of operations in accordance with generally accepted accounting principles. Basic financial report requirements include the following:

- The Combined and Combining Balance Sheets - All Fund Types;
- The Combined Statement of Revenues, Expenditures and Changes in Fund Balances - All Governmental Fund types;
- The Combined and Combining Statement of Revenues, Expenditures and Changes in Fund Balances, Budget and Actual - All Governmental Fund types;
- The Combined Statement of Revenues, Expenses, and Changes in Retained Earnings All Proprietary Fund Types;
- The Combined Statement of Cash Flows - All Proprietary Fund Types. (The Statement of Cash Flows may be reported using the direct or indirect method of cash flows from operating activities. Although GASB encourages the use of the direct method of reporting cash flows from operations, entities may utilize the format considered the most informative. The format chosen for the annual report is the Indirect Method.)

VI. INTERNAL CONTROL

Internal control is recognized as fundamental and indispensable to all types of organizations. It can be defined in terms of two elements, administrative controls and accounting controls. Administrative controls are designed to encourage adherence to prescribed policies and accounting controls deal with safeguarding assets.

Both administrative and accounting controls are implemented primarily through:

- Developing specific written procedures that specify how activities and functions will be conducted;
- Segregating key control duties and responsibilities among different employees;
- Monitoring these procedures, duties and responsibilities to ensure conformance over time.

The grantee is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by the grantee are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of internal control are to provide the grantee with reasonable, but not absolute, assurance that assets are safeguarded against loss and that transactions are executed in accordance with the grantee's authorization.

In the financial operation of CDBG funds, it is presumed that, as a minimum, the grantee will see that the work is properly segregated so that no one person is allowed to perform a complete cycle of operations. Where segregation of duties is not always possible because of staffing limitations, management should function in an oversight capacity. In such an event, the oversight provided should be as compensating as circumstances permit.

Internal Control may not eliminate the probability that errors or irregularities will occur. But the probability of their occurrence can be reduced if the grantee will put in place the proper administrative and accounting control policies and procedures.

CHAPTER 4

EXHIBITS

- 4-A Budgetary Authority Resolution**
- 4-B Allowable and Unallowable CDBG Administration Costs**
- 4-C Request for Funds Form Instructions and Form**
- 4-D Directions for Using the Uniform Status of Funds Spreadsheet and Spreadsheets**
- 4-E Directions for Using the Uniform Invoice Tracking Spreadsheet and Spreadsheets**
- 4-F Project Progress Reports**
- 4-G Federal Regulations for Real Property**
- 4-H Program Income**
- 4-I Expenditure Review**
- 4-J Program Income - Title I Certification**
- 4-K BARS Chart of Accounts Excerpts**
- 4-L Sample Construction Project Chart of Accounts**
- 4-M Chart of Accounts for State/Federal Projects**